EU Banking and Finance Regulatory Newsletter - Spring Edition 2021

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Spring has sprung and the EU-UK Trade and Cooperation Agreement has been done. Even with this deal ratified and applying in full from May 1, 2021, rifts are still rumbling on both sides of the divide amongst the now quite familiar topics. From differing views on vaccination shipments to fishing quotas, the outlook for a comprehensive building of new bridges on financial regulatory cooperation or least mutual market coexistence is still fragile. The efforts on the planned regulatory memorandum of understanding still stops short of equivalence. Diverging standards on everything from the future direction of supervision of crypto-assets, artificial intelligence (see our coverage on these new rules) to ESG methodology, as well as UK tweaks to MiFID research rules or to EU "quick fix" legislation that was previously on-shored in the UK is driving fragmentation.

Economic growth across Europe is currently diverging as different stages of lockdown are taking varied directions, thus making it potentially tricky for the ECB to communicate and signal as clearly in terms of its toolkit. Crucially, however Germany's Constitutional Court gave the green light to approve domestic legislation ratifying the EU's recovery Fund having dismissed the legal challenges against the common debt funded investment plan that is backed by the EU's budget.

Meanwhile the European Commission and the European Insurance and Occupational Pensions Authority (EIOPA) as well as industry on April 29th started discussing options to improve protections of businesses affected by the COVID-19 pandemic notably as the withdrawal of state-led support measures will likely reveal the extent of full damage caused by the health and economic crisis that the EU and its Member States have been weathering. Insurers and reinsurers are like the banks, expected to be part of the solution. The European Systemic Risk Board warned on April 28th that "The threat of a wave of insolvencies looms large, unless Member States manage a smooth transition from liquidity support towards more targeted solvency support and successful corporate debt restructuring for viable firms."

This is not the first time that the ESRB (along with the almost monthly statements from the ECB) have called for greater Fiscal action and coordination and is particularly timely as most Member States have sent in their national recovery and resilience plans to the European Commission (by today, April 30) as well as to their national parliaments. France and Germany have presented a joint plan and across the board these national plans, which are essential to the delivery of the EU's €750 trillion Recovery Fund efforts include ambitious structural reforms. These range from tax to national labor market improvements as well as to push infrastructure improvements, increased digitalization and the greening of the economy thereby delivering further components of the Green Deal. As soon as the individual Member State's plans are approved, countries are entitled to receive up to 13% of their allocated funds as advance payment – possibly by the start of summer. All of this goes hand in hand with the EU's unveiling of its new Industrial Strategy, which in turn is expected to further complete the Single Market as well as the path for recovery.

The start of spring and the publication of the ECB-SSM's Report on its Targeted Review of Internal Models (**TRIM**)

multiannual review that started in 2016, which was carried out at 65 significant credit institutions throughout more than 200 on-site investigations, may cause a lot of spring cleaning across the banking sector as a whole and not just those that were in-scope. The SSM concluded that "TRIM confirmed that the internal models of [systemic institutions] can continue to be used for the calculation of own funds requirements, subject to supervisory measures to ensure an appropriate level of own funds requirements at all times". However, the "relevant supervisory measures" that banks must now implement are based on supervisory ''findings'' – items requiring immediate supervisory attention – with the ECB-SSM identifying more than 5,800 findings across all risk types, of which approximately 30% were considered as having high or very high severity.
The ECB-SSM's Report equally, perhaps more tellingly, provides a detailed overview of findings regarding general topics; credit risk; market risk; and counterparty credit risk. To address these findings, the ECB-SSM is able to issue binding supervisory decisions containing obligations, or remedial action needed to achieve compliance with a legal requirement.

Given that 75% of all obligations have an implementation period of over 12 months, some limitations (which restrict or modifies the permitted use of a model) may be required in cases where noncompliance led to an underestimation of capital requirements. Overall, 253 supervisory decisions have been, or are in the process of being, issued. Of these, 74% contain at least one limitation and 30% contain an approval of a material model change.

In summary, the ECB-SSM stated that the TRIM project had "fully achieved" its main objectives of reducing non-risk based risk-weighted assets (RWA) variability and supporting future supervision of internal models across the SSM. Overall, it is expected that the supervisory decisions will "…lead to a 12% increase in the aggregated RWA covered by the models assessed in the respective TRIM investigations. This corresponds to an overall absolute RWA increase of about €275 billion as a consequence of TRIM and to a median impact of -51 basis points and an average impact of -71 basis points on the CET1 ratios of the in-scope institutions." TRIM was the ECB-SSM's first big project that has now a potential to deliver a big impact. It is quite conceivable, and notably with a view to the ECB and SSM's priorities for 2021 and 2022 that the "success" of TRIM will push for similar types of projects going forward.

We hope you enjoy this month's edition. Further analysis on some of the developments above are in this month's Thought Leadership section as well as available on our Eurozone Hub. If you find yourself reading someone else's copy and wish to be added to the circulation list, please send an email to eurozone-hub@dentons.com **and we will do our best to make sure that you will get the next edition and all future editions. It goes without saying that if you have any feedback to give us in relation to this monthly newsletter – positive or negative – we would be delighted to hear from you.**

Regulatory developments in the EU

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We present you with a selection of key regulatory developments in the EU.

Regulatory developments in Germany

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We present you with a selection of key regulatory developments in Germany.

Regulatory Developments in Spain

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Regulatory Developments in Italy

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Regulatory developments in Luxembourg

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Regulatory developments in the Netherlands

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Regulatory developments in the Czech Republic

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We present you with a selection of key regulatory developments in the Czech Republic.

Regulatory developments in Romania

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We present you with a selection of key regulatory developments in Romania.

Our recent Thought Leadership

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The following represents a carefully curated selection of our recent Thought Leadership contributions.

Global Financial Markets Regulatory Review - April 2021 Edition

Global: Dentons is pleased to present the April 2021 edition of the Global Financial Markets Regulatory Review. The report combines insights from Dentons lawyers with extensive financial markets experience located in major global financial centers. The reports for each country include links to further information and contact information for Dentons professionals.

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